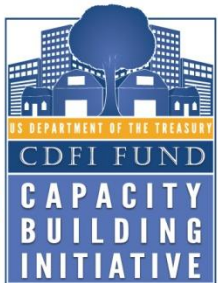




Applying the 5 Cs to Food Production Loan Applicants

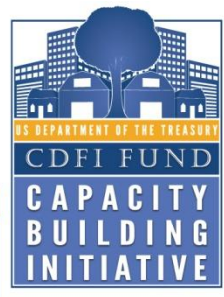
Dorothy Suput, The Carrot Project

Denise Dukette, Lead Trainer for FHFO Food Production Workshops



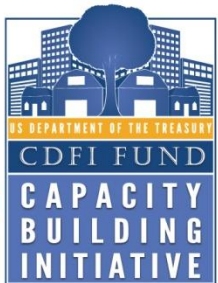
Introduction

- CDFI Fund's Capacity Building Initiative
 - Financing Healthy Food Options
 - Workshops
 - Technical Assistance
 - Resource Bank



Today's Webinar Topic

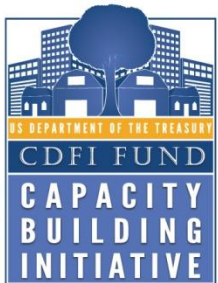
- Food production loans require a re-definition of the 5 C's of credit
- Real-life applications of this criteria to actual farm loans
- See results after two years and learn key take aways from practitioners in the field



Dorothy Suput

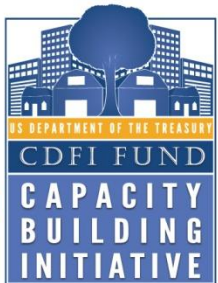


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THE carrot PROJECT

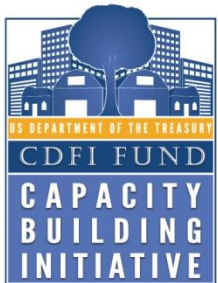
Creating small-farm financing solutions



Denise Dukette



Vice President
New England Bank
ddukette@live.com

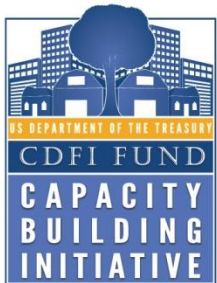




Applying the 5 Cs to Food Production Loan Applicants

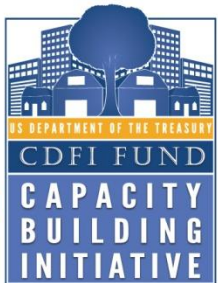
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Agenda

- The 5 C's of Credit – re-defined
- Case studies
 - SeaSaw Farm
 - Hill Town Farm
- Take Aways

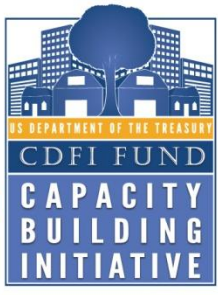


5 C's of Credit – Redefined!

- The 5 C's are common tools for lending
- Typically they are evenly weighted to make lending decisions

We redefine them:

to reflect the realities of the small farm production sector and to better weight them to this sector's risks



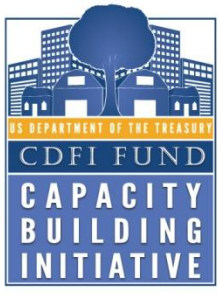
The 5 C's Redefined:

Primary Factors

- Cash Flow Modeling
- Capacity/Character:
Farm Management
Skills
- Conditions: Know the
Market

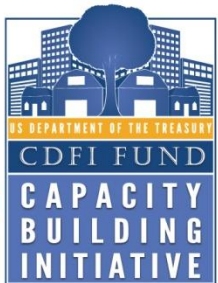
Secondary Factors

- Cash/Equity
- Collateral



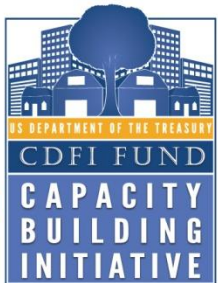
Primary vs. Secondary

- Primary factors may be deal breakers. They are critical to success.
- Primary factors identify skill and knowledge gaps which may require TA.
- Secondary factors help fine tune a loan decision but do not “fix” issues with primary factors.



Primary

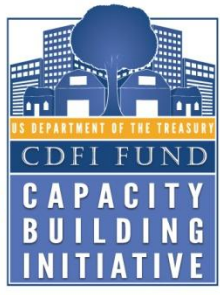
- Cash Flow Modeling – know the cash flow!
- Capacity/Character: Farm Management Skills – not a day job!
- Conditions: Know the Market – if you grow it, you need to sell it!



Cash Flow Modeling

Cash Flow Repays Loans!

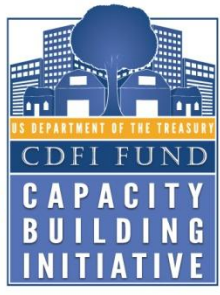
- The loan needs to create increased cash flow in some way – crop diversity, yield, growing season, acreage, access to new markets
- Applicant's viability is likely **not** based on historic performance or independent cash flow support
- Viability is based on taking agriculture experience to a new level (products, growing methods, scale, etc.)



Cash Flow Tools

Combine products in baseline cash flow

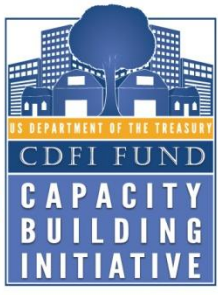
- Need to overlay each existing major product cycle into cash flow
- Overlay new product cash flows into cash flow model
- Monitor overall cash flow as well as by product
- Look for cash flow issues in core operation
- Assess profitability of product lines – not just of aggregate model



Cash Flow Tools

Combine products in baseline cash flow

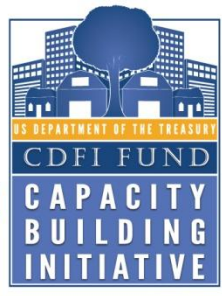
- What will loan accomplish? Pro forma cash flow model
- Capital expenditures for planned production; long term viability
- Unplanned expenses – disease control, weather, vet bills, repairs, equipment breakdown, increased utility costs
- Major variable costs – fuel to transport product, “raw materials”, fertilizers/feed



Farm Management Skills

Range of critical skills is broad and highly specialized:

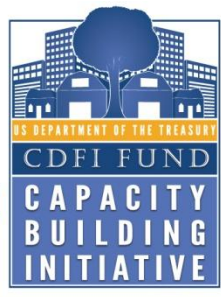
- **Product Expertise** – raise/grow product, weather, disease/ illness, changing demand, product development
- **Marketing** - identify markets, determine accessibility, product and sale requirements, payment cycle and method
- **Practical Skills** - equipment maintenance, mechanical ability, resourcefulness
- **Logistics** - get to market, route density, accessible markets



Farm Management Skills

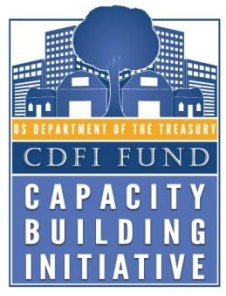
Range of critical skills is broad and highly specialized:

- **Staffing** - seasonality, cost, housing, payroll processing
- **Financial Management** – cost controls, cash flow modeling, financial reporting, invoicing and receivable collection, budgeting
- **Capital Needs** – understanding equipment/facility needs
- **Regulation** - regulatory, zoning, land use requirements
- **Sector Knowledge** – changing requirements, regional and national trends, food habits



Farm Management Skills

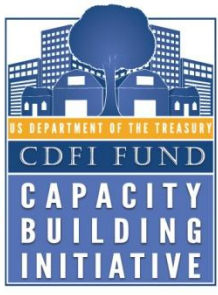
- No single skill will provide the basis for success but lack of a critical skill can be a recipe for failure
- A good farmer-borrower is a risk-taker, identifies unmet needs, and expands/adapts to fill that gap in an appropriate and planned way
- Entrepreneurial spirit is critical to successful small farms which must continually adapt to a changing marketplace and landscape



Know the Market

Farm scale may dictate the market; market accessibility may also direct farm scale.

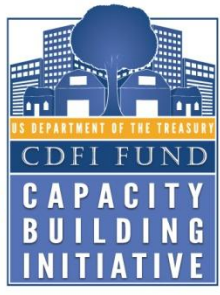
- Strong marketing skills necessary to assess and gain entry to new markets
- Must identify optimal markets, determine proper pricing, obtain contracts, ensure that delivery goals are met
- Lack of aggregation and distribution infrastructure places burden on farmer to develop marketing approach and logistics planning get to market.
- Cooperative approach may be achieved but requires development of marketing approach and logistics strategy among participants



Know the Market

Assessing applicant's ability to get to market:

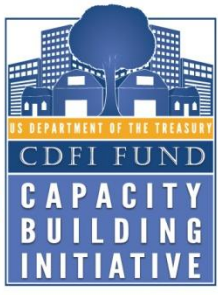
- How shelf stable is the product? Can it be stored for future sale or is it highly perishable?
- What volume is being produced for sale, within a saleable timeframe?
- Distance to sell product? Adequate delivery vehicles or sell on-site and expect a reasonable demand?
- How strong is the demand for the product? Geographic reach? How does price vary within the region? Are there buyer groups who will pay a premium or create consistent demand? Are there institutional buyers who will purchase in bulk?



Know the Market

Assessing applicant's ability to get to market:

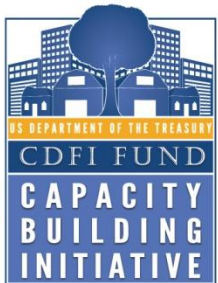
- Are there any selling groups or aggregation/distribution organizations which can provide a larger marketing outlet for the individual?
- How do target customers typically pay? Under contracts, open account, credit card, COD, cash, etc.
- What markets are being sold into – retailers? Restaurants? Consumers? Institutions? Each will have requirements for quality, volume, timeliness, payment methods, and timeline for payment as well as risk of non-payment.



Secondary Factors

Why Are These Secondary Factors?

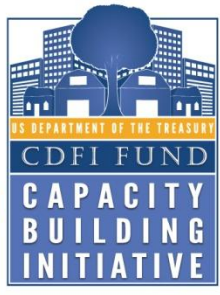
- Not direct indicators of potential success; are fallback positions
- In a young and emerging sector, are least likely to be present in a financing application
- Reliance on fallback reduces emphasis on critical support needs
- Over-weighting will eliminate consideration of viable opportunities



Secondary Factors

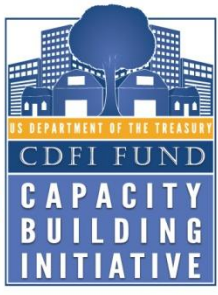
Rather, success is driven by active support network to access critical resources as needed

- Very few small farms find appropriate resources on their own; they need TA
- Farmer's strongest skills are specific agricultural or husbandry niche, not necessarily business skills



Secondary

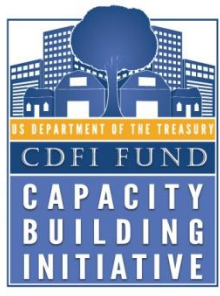
- Cash/Equity – Do you have liquidity to carry a farming loss?
- Collateral – Can you sell assets to generate cash or repay debt?



Cash/Equity

- Small farms typically boot-strap
- Use credit cards for purchases; pay after seasonal sales
- Liquidity is net cash after products sold and bills paid
- Funds are reinvested in the farm; farmers live on limited budget and do not build liquidity
- Farmer and farm are one financial entity; no fallback
- Farmer is core employee – illness or interruption affects production and cash flow

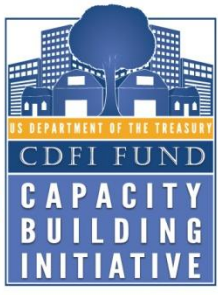
Lending goal is to strengthen farm cash flow and ensure farm viability and living wage for farmer/family



Cash/Equity

Mitigants

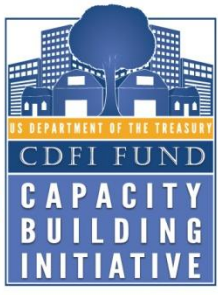
- May have sweat equity versus cash contribution
- May have co-signer or guarantor
- Fully committed to farming and farming lifestyle
- Can accept and make full use of TA help
- Can adapt to changing environment
- Can leverage growth in sector through entrepreneurial spirit



Collateral

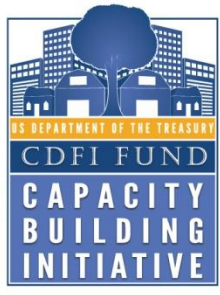
Collateral should be obtained if available BUT is unlikely to be a strong loan fallback if repayment fails

- **Value in farming is of the value of the final product, in its best state of health**
- Maximum asset value is as “going concern” enterprise
- Removal of assets may directly impair farm production
- Interrupted growth cycle may impair product value (i.e., wilted produce, unhealthy livestock)

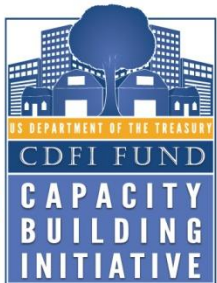


Keys to Overall Success: Engage with the Sector

- *Get to know the Ag sector in your communities:* a strong TA program and network of agricultural service providers help lenders evaluate risk and ultimately help the borrower to obtain credit.
- *Base lending decisions on appropriate lending benchmarks and measures,* weighted to the realities of this sector.
- *Test the fundamentals:* cash flow, market knowledge and conditions, farm management and production capacity.



Our Clients



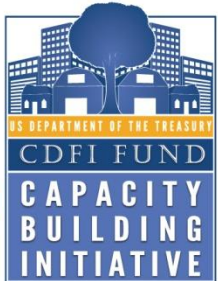
THE **carrot**
PROJECT

Creating small farm financing solutions

Provided by **OPPORTUNITYFINANCE**
NETWORK

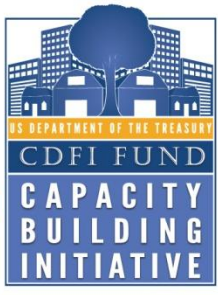
SeaSaw Farm

- **Purpose of Loan:** Purchase and installation of bread oven for bakery in new location, \$15,000
- **Farm Description:** Community farm store and concert venue, bread bakery, pork, beef, milk and year-round greens
- **Acreage:** 146 acres total, with 100 in pasture and vegetables, and the remainder in forestry.
- **Years in Business:** Recent merger on newly purchased farmland between established bakery and dairy (2 years) and year-around greens. Plan on forming an LLC.



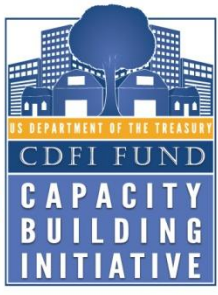
SeaSaw Farm: Financials

- **Projected Gross/Net Income:** First season, \$130,000/\$70,000 to be invested back in business
- **Debt:** Little equity in farmland and buildings valued \$225,000 with a 20-year loan of \$180k and additional \$55k in friends and family loans to be paid in product
- **Collateral:** Possible \$35k in equipment and vehicles, other business and personal assets with a total net value of \$275,000



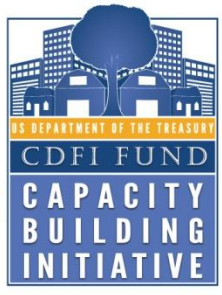
SeaSaw Farm: Cash Flow

- Provided projected enterprise budgets for all products aggregated for entire operation for 3-years with monthly breakdown
- Anticipated growth from bakery, which was already established, and new business from year around greens sales
- Of two-owners, one would not take a draw in the first few years; instead off-farm salary is invested in business
- Debt Service was about 1.2 including off-farm income



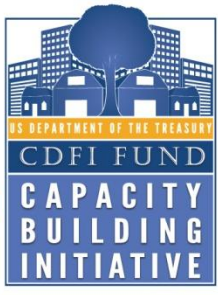
SeaSaw Farm: Farm Management Skills

- Combined 16 years of experience farming with specific expertise:
 - One owner ran bakery and dairy for several years prior to merger
 - The other managed college farms and was an educator, training on farm operation and management of diversified vegetable operations
- Commitment to staying on top of financials and using information to actively managing the direction of their farm



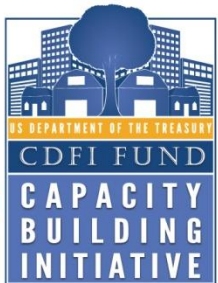
SeaSaw Farm: Market Conditions

- Dairy and bakery had a 2-year history and established customers
- Located in food active area of state and near major population center
- Strong target customer base for Local Food Club, built on customer base for milk and bread
- No competition for local winter greens; summer greens expand offerings in Farm Share store
- Meeting unmet demand for locally-raised meat and raw milk



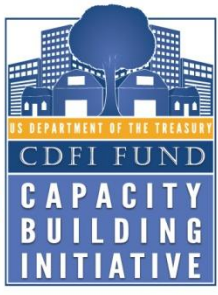
SeaSaw Farm: Cash Flow Analysis

- Off-farm income provided critical cash flow in early years
- Cash on hand provided financial cushion
- Family and Friend loans being paid back in food needed to be factored in and accounted for
- Projections for greens seemed too aggressive
- Projected bread price was above market; needed to be tested. If mis-priced, directly affects cash flow.



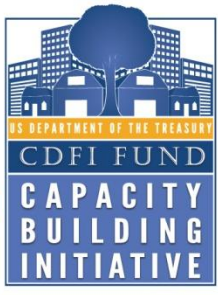
SeaSaw Farm: Management Skills Analysis

- Farmers had experience running similar operations; one had run a farm operation
- Provided a thoughtful and thorough farm plan
- Successful in highly competitive process to buy land from land trust
- Business merger brought two owners together with little experience co-managing, but with clearly articulated roles and responsibilities and understanding of each other's strength's and weaknesses



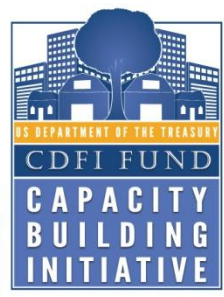
SeaSaw Farm: Market Conditions Analysis

- Thoughtful analysis of market options
- Year-around greens created new opportunity in market
- Establishment of store as center of Local Food Club with events was creative (concert hall) (*and risky!*)
- Unique product mix meeting unmet needs with protein, dairy, bread, and vegetable combination
- Bread price point proved realistic on further analysis
- Supportive customers had already provide friends and family loans; farmers had good reputation among customers



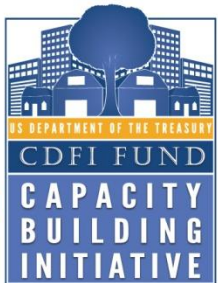
SeaSaw Farm: Secondary Factors

- Strong cash position for a new business with off-farm income; reinvestment in business; and established customer base
- Committed to building equity through re-investment of off-farm income; payment of friend & family loans in product
- Possible collateral was mix of farm equipment and vehicles, but primarily personal assets



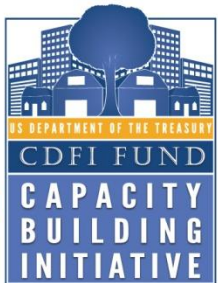
SeaSaw Farm: Loan Decision

- Approved 5-year, \$15,000 loan with no conditions
- Monthly payments of principal and interest throughout year (not seasonal)
- Fixed interest rate of 5.75%
- Security interest in all business assets



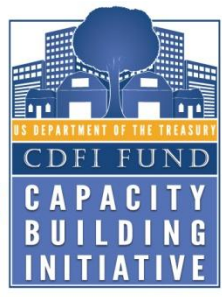
SeaSaw Farm Results: 2 Years Later

- Made the loan for \$15,000 for 5 years; payments are current
- Subscription-based Local Food Club, direct sales through the farm store, farmers' markets, wholesale accounts going well
- Innovative one-time event that took off: 'Pizza Night' became established part of business with 400+ customers on summer evenings
- Pizza Night success caused owners to re-analyze business and adjust time and expectation to making it work
- Both owners now working full-time on farm



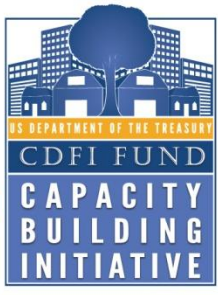
SeaSaw Farm: Takeaways

- Farm had fundamentals in place to support financing request
 - Strong management
 - Established customers
 - Off-Farm income
- Financing request was for specific item; easy to define and analyze
- Innovation (greens, Pizza Night) showed entrepreneurial spirit but also added risk



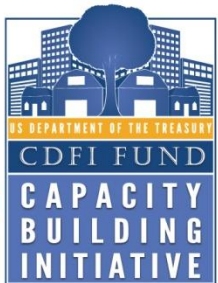
Hill Town Farm

- **Initial Loan Request:** \$20,000 to: 1) expand fruit production and value-added products, 2) improve native habitat for wildlife and pollinators, 3) increase agro-tourism
- **Farm Description:** Forest and field fruit production, heirloom vegetables, fruit-based value-added products
- **Acreage:** 50
- **Years in Business:** 2 years – developing business and idea, test markets, and developing products



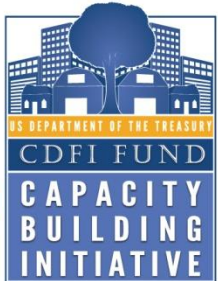
Hill Town Farm: Intervention

- At pre-qualification stage, recommended business planning class with the goals of:
 - Focusing business on most promising enterprises
 - Developing more detailed cash flow
 - Reconsider goals and purpose of loan request
- **Final Loan Request:** \$15,000 after completing business planning course and refining plans (3-month interval)



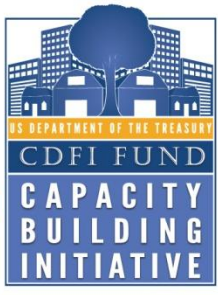
Hill Town Farm: Financials

- **Projected Gross/Net Income:** \$30,000/\$21,000
- **Off-farm Income:** \$15,000
- **Debt:** Co-owned mortgage of \$325k, \$30K in student loans; second property on-market proceeds to buy-out co-owner and then apply to other debt
- **Collateral:** \$175k equity in the co-owned farm, house, and buildings; exclusive ownership of vehicles and small farm equipment
- **Equity:** \$20k in farm infrastructure



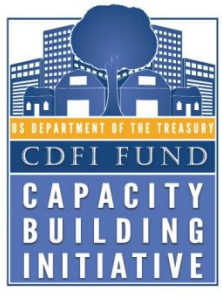
Hill Town Farm: Cash Flow

- Detailed cash flow by sales outlets and products; exhaustive on possible expenses; projections for three-years, by month with limited historical data
- Did not account for seasonal production or lag between harvest and finished value-added product
- Very aggressive projections



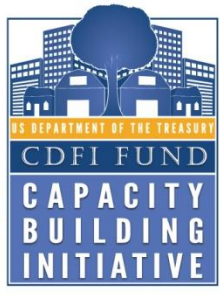
Hill Town Farm: Farm Management Skills

- 2-years of growing experience plus strong academic background and practice in horticulture
- Business experience in running Bed & Breakfast
- Built connections to cooperative extension for experimental trials on farm
- Skilled marketer
- Dislikes bookkeeping and financial planning



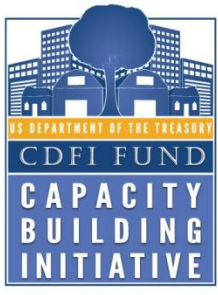
Hill Town Farm: Market Conditions

- Unique products including elderberry, black currants, and value-added products
- Little local or organic competition in products
- Test-marketed for two years at farmers' markets and test samples at restaurants and specialty stores
- Moving from home to commercial kitchen to increase batch sizes, and gain access to a co-packer and storage



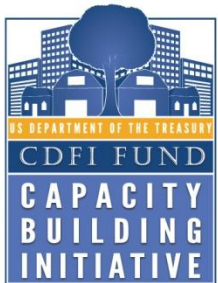
Hill Town Farm: Cash Flow Analysis

- Straight lined expenses that didn't reflect seasonal fluctuations in input needs, labor, harvesting, use of commercial kitchen, etc.
- Aggressive projection for new value-added products and new markets
- If projections were accurate or conservative as owner discussed, then cash flow positive
- Debt Service range from below to 1.2 depending on assumptions
- Possible to delay payments on portion of debt load



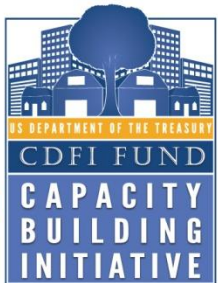
Hill Town Farm: Management Skills/Character Analysis

- Commitment to learning was evident
- Strong small business and marketing skills
- Weaker in financial management
- Investment in learning about crops and 'listening to the land' in terms of what it grows best
- Limited experience with specific crops and value-added products
- Diversion and uncertainty with need to buy out co-owner and possible options



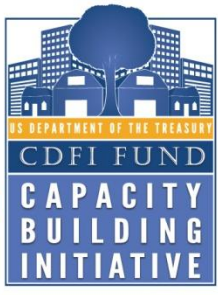
Hill Town Farm: Market Conditions Analysis

- Native berry selection and related products filled market niche
- Value-added has shelf life and potential to even out cash flow with growth
- Potential for local and statewide and regional distribution of value added product



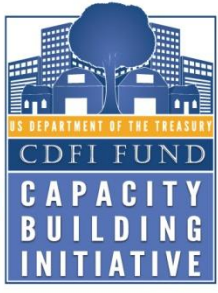
Hill Town Farm: Secondary Factors

- **Cash/Equity:** Value of equity was in transition because of potential sale of second-property and buy-out of co-owner
- **Collateral:** Possible was greater than \$15,000 loan including car, equipment, greenhouse



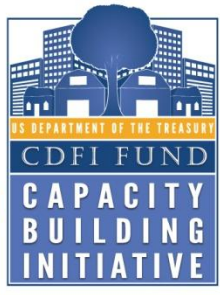
Hill Town Farm: Loan Decision

- Conditionally approved \$15,000 loan for 5 years, 5.75% with satisfactory responses to the following:
 - Basis for aggressive projections for first value-added product; How business would address accounting and bookkeeping needs; Clarification of collateral; More information on arrangements and expectation of co-owner of farm property
- Strong mission fit and possibility for huge success
- Security interest in all business assets of farm owner
- Use of a guarantee pool



Hill Town Farm: Results: 2 Years Later

- Loan paid off early
- Products and marketing strategy have done very well
- Loan contributed to building several new products
- Became 'established' so could apply for a loan to buy out co-owner from USDA-FSA
- Building commercial kitchen on property; moving out of off-site commercial kitchen
- Continued with business planning assistance
- Working with State on marketing of specialty products
- Planning for transition of farm and business to next generation



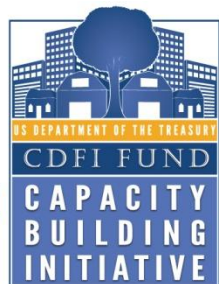
Hill Town Farm: Take Aways

- This was not a slam-dunk, but a great mission fit
- Directing applicant to business planning support services and continual effort by owner to build support network for business extremely beneficial, e.g. hiring a bookkeeper, working with State marketing specialists
- This was a character loan based on an unproven but sound business idea and a bet on the cash flow
- The process to make a decision on the loan was complicated and required revisions and through justifications from owner



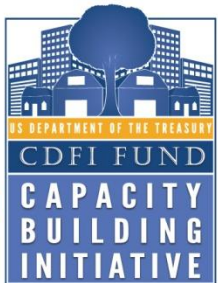


Questions?





Additional Resources



Financing Healthy Food Options Resource Bank

http://www.cdfifund.gov/what_we_do/FinancingHealthyFoodOptionsResourceBank.asp

CDFI Fund - U.S. Treasury - x

← → ↻ www.cdfifund.gov/what_we_do/FinancingHealthyFoodOptionsResourceBank.asp

- WHO WE ARE
- WHAT WE DO
- IMPACT WE MAKE
- NEWS & EVENTS
- HOW TO APPLY

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

UNITED STATES DEPARTMENT OF THE TREASURY



Financing Healthy Food Options Resource Bank

I. Training Curriculum

- [Food Systems Overview](#)
- [Healthy Food Retail Financing](#)
- [Financial Services for Mid-Tier Food Chain Enterprises](#)
- [NMTC & Urban Supermarkets](#)
- [Understanding the Grocery Industry](#)
- [Underwriting Supermarkets & Grocery Stores](#)
- [Mid-Tier Food Chain Enterprises Overview & Underwriting](#)
- [Capitalizing Healthy Food Retail Initiatives](#)
- [Identifying Optimal Areas for Supermarket Development](#)
- [Understanding the Food Production Sector](#)
- [Credit Skills for Lending to the Food Production Sector](#)
- [Food Producers Case Studies](#)
- [Identifying Partners and Convening Stakeholders](#)

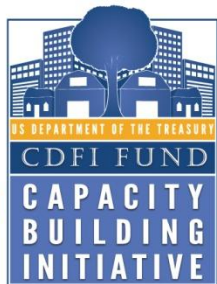
II. Training Webinars

III. Additional Resources

- Searching for Markets: The Geography of Inequitable Access to Healthy and Affordable Food
 - [Executive Summary](#)
 - [Full Report](#)
- [Financial Resources Catalogue](#)

IV. Food Desert Mapping Tools

- [USDA Food Desert Locator](#)
- [PolicyMap](#)



Financing Healthy Food Options Webinar Archive

http://www.cdfifund.gov/what_we_do/FHFOResourceBankWebinars.asp



The screenshot shows a web browser window with the URL www.cdfifund.gov/what_we_do/FHFOResourceBankWebinars.asp. The page features a navigation menu on the left with links: WHO WE ARE, WHAT WE DO, IMPACT WE MAKE, NEWS & EVENTS, and HOW TO APPLY. The main header reads "COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND" and "UNITED STATES DEPARTMENT OF THE TREASURY". Below this is the CDFI Fund logo and a section titled "Financing Healthy Food Options Resource Bank: Webinars". A note states: "Relevant Training Curriculum chapters can be found on the Resource Bank's [main page](#)." The page lists four webinar topics with associated resources:

- 1. PolicyMap and Using Limited Supermarket Analysis in Your Target Market**
 - [Webinar 1 Presenter Biography](#)
 - [Webinar 1 Accompanying Presentation](#)
- 2. Healthy Food Options Program Design and Social Impact Measurement**
 - [Webinar 2 Presenters Biographies](#)
 - [Webinar 2 Accompanying Presentation](#)
 - [Sample Retail Loan Pre-Application Design](#)
 - [Sample Retail Loan Application Design](#)
 - [Sample Retail Loan Template for Data Collection \(.xls\)](#)
 - [The Grocery Gap: Who Has Access to Healthy Food and Why it Matters \(Food Trust and PolicyLink\)](#)
- 3. Green for Greens**
 - [Webinar 3 Presenters Biographies](#)
 - [Webinar 3 Accompanying Presentation](#)
 - [Green for Greens: Finding Public Financing for Healthy Food Retail \(Public Health Law & Policy\)](#)
 - [Getting to Grocery: A Toolkit for Attracting Food Retail to Underserved Neighborhoods \(Public Health Law & Policy\)](#)
- 4. New American Foodshed**
 - [Webinar 4 Presenters Biographies](#)
 - [Webinar 4 Accompanying Presentation](#)
 - [Field Guide to the New American Foodshed](#)
 - [Field Guide: One Page Planning](#)
 - [National Good Food Network](#)
 - [Farm Credit Council](#)

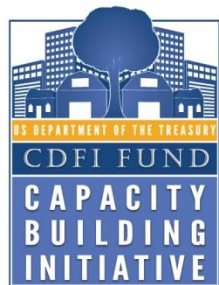


Upcoming TA Webinars

Chips to Carrots: Financing Healthy Corner Stores

•Thursday, September 27 @ 2pm EDT

Visit www.opportunityfinance.net/FHFOwebinars/ to register for one or all of the TA webinars



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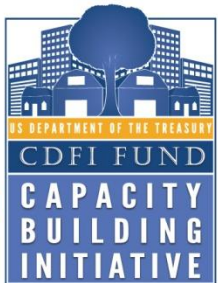
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Applying the 5 Cs to Food Production Loan Applicants

Dorothy Suput, The Carrot Project

Denise Dukette, Lead Trainer for FHFO Food Production Workshops

